

Interview by Vinson and Elkins  
with Kelly Salt  
at footnote(s):

927, 928

M E M O R A N D U M

April 2, 2004

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TO: Paul S. Maco  
Richard C. Sauer

FROM: Amy Nieset Drew

RE: *City of San Diego*; Interview of Kelly Salt

This memorandum summarizes the interview of Kelly Salt. This memorandum does not contain a verbatim or a near-verbatim transcription of this interview, but rather is a general summary of my thoughts and mental impressions regarding our discussions. Significantly, it is organized to summarize issues thematically, and does not reproduce the order in which the interview actually occurred. There was no stenographer present at this interview, and given the nature of summarizing this type of discussion after the fact, it does not attempt to describe every statement or exchange and it is possible that there are errors in this account. It also assumes familiarity with the facts of this case, and does not provide context or explanation of every factual reference. Nor does it address issues of credibility or attempt to reconcile any differences in the accounts of other individuals.

This memorandum is subject to the attorney-client and the work product privileges, as it was prepared in connection with our providing legal advice to the city of San Diego (the "City") in connection with a potential SEC and U.S. Attorney investigation regarding some of the matters discussed in this memorandum.

Mr. Maco began by explaining the informational purpose of the interview and informed Ms. Salt that the information gathered would be used by Vinson & Elkins in its internal investigation into various matters related to errors in the City's financial statements and bond disclosures. Mr. Maco further explained that the eventual report created in the investigation would likely be given to the Securities and Exchange Commission as well as the Department of Justice. Ms. Salt was told that she would be provided with a copy of this memorandum for review and comment. Finally, Mr. Maco explained that Vinson & Elkins represents the City of San Diego and does not represent Ms. Salt personally.

*General overview of interview.* Paul Maco and I met with Ms. Salt for approximately one and a half hours on March 24, 2004. Ms. Salt was very helpful and willing to provide answers and some additional documents responsive to questions asked. Ms. Salt began with a brief history of her personal involvement in the City's bond issuances. Next, she discussed the

mechanics of a bond issuance, including the engagement of bond counsel, the drafting of the Official Statement (OS), and the review of bond documents by any relevant departments. Ms. Salt also explained the way that bond issuances were approved by City Council ordinance and resolution, as well as which kinds of documents are approved by ordinance and which are approved by resolution. Next, Ms. Salt explained the process for presenting a bond offering to the City Council and the process by which the Council reviews and ultimately decides upon an issuance.

Ms. Salt works closely with the Public Facilities Financing Authority ("PFFA"), the joint-powers authority that nominally issues debt on behalf of the City. Ms. Salt described the PFFA and its procedures for issuing bonds. She also briefly described the other authorities that issue bonds for the City.

It is important to note that throughout the interview, Ms. Salt frequently referred to the City as the issuer of bonds. Generally, under California law, the City may not issue long-term debt directly, without a prior approving 2/3 vote. Thus, the obligations covered in our discussion were often issued by the PFFA and not directly by the City. The City's tax anticipation notes are handled by another attorney in the City Attorney's Office and not by Ms. Sals.

*Ms. Salt's background.* Ms. Salt is an attorney in the San Diego City Attorney's Office whose duties involve preparing bond issuances for the City. The first offering she worked on was the trolley extension financing with Curtis Fitzpatrick and Mary Kay Jackson. That financing was accomplished under a joint powers authority made up of the City and the Metropolitan Transit Board.

Next, Ms. Salt was involved with the first issuance of sewer revenue bonds in 1993. Those bonds were issued following litigation involving the city and the Environmental Protection Agency over National Pollution Discharge Elimination System permits and violations. That litigation led the City to enter into a Consent Decree requiring conversion to a secondary waste treatment process. This conversion was estimated to cost approximately \$1 billion, leading the City to decide to finance the conversion through a bond issuance. Dennis Kahlie evaluated the needs for the capital program and developed the rate case.

Next, Ms. Salt worked on the Chargers stadium expansion financing. Finally, she worked on a number of financings, including the financing of the City's water system upgrades.

*Mechanics of a bond issuance.* Once the City decides to issue bonds for a project, Ms. Salt is contacted to engage outside bond counsel, possibly through a Request for Proposal ("RFP") process. Bond counsel provides a shell of an OS based on past offerings, outlining issues that City departments need to address. Relevant departments then flesh out the details from this outline. Different departments participate in the drafting depending on the nature of the financing. For example, an OS involving wastewater would need to be drafted by that department because of the necessity of familiarity with the past litigation between the City and EPA. Ted Bromfield might participate, for example, on behalf of Wastewater Department.

After a department has filled in the details in the OS outline provided by bond counsel, the information is sent back to bond counsel, who prepares a draft OS. This draft is then

distributed among the parties who have the knowledge base to review it for accuracy. This review, by as many as 15 various knowledgeable parties, is coordinated by a Project Manager from Financing Services. After reviewing the draft OS, these various parties either forward their comments directly to bond counsel, or to the Project Manager if the Project Manager wishes to provide bond counsel with a cumulative response. Examples of past project managers include Mary Vattimo for the stadium expansion, Elizabeth Kelly and Jeff Witt for the ballpark financing, and Dennis Kahlie for wastewater and water.

Once bond counsel receives, assembles, and integrates all comments on the draft OS, a series of all-hands meetings with city officials, bond counsel, and underwrites, begins. These meetings, once done in person, now frequently take place over phone and through email. At some point in these meetings, a page-turner is done to ensure that everyone is able to comment on the draft. It is important to note that a similar process is used for review of bond documents in addition to the OS.

At the conclusion of this review and comment phase, a complete, agreed-upon document emerges. If this document is a bond document with a revenue or general fund liability of more than five years, it will need to be approved via ordinance by the City Council. If the document is a preliminary OS, which does not have its own financial obligation, it will be approved by the City Council via resolution.

***Ordinance versus resolution.*** Bond documents with revenue or general fund liabilities in excess of five years must be approved by City Council ordinance. Procedurally, an ordinance must be introduced, or read, twice. A first reading takes place then, no sooner than 10 days later, a second reading. Following the second reading, there is a 30 day referendum period, after which the ordinance is effected. Bonds may not be sold until the conclusion of this process. There is also a 60-day referendum period pursuant to the Government Code, but it can run concurrently with the 45-day period.

Documents like the OS, which do not carry their own financial obligations, are approved by Council resolution. Because the resolution process does not have the same time requirements as the ordinance process, it is frequently the case that the ordinance process for finalized bond documents is begun while the OS is still being revised.

***City Council approval for a bond issuance.*** A bond document intended for City Council ordinance approval is guided through the approval process by the 1472 Request for Council Action routing document ("1472 form"). This document provides fund numbers and accounting details for the offering as well as an explanation of all documents being provided attached to it, like a Master Installment Purchase Agreement and a City Council resolution, if one is being requested along with the ordinance. Attached to the 1472 form is a document called the "A Page" or "Manager's Report" which is a description of the offering provided by the Project Manager from Financing Services.

Also attached to the 1472 form are drafts of the bond documents. The 1472 form provides for routing of these documents to all parties whose signatures are required for approval, including the City Auditor, the City Attorney, a representative responsible for environmental review, a representative from the City Manager's office, and other parties depending on the

nature of the financing. The 1472 form has signature and date spaces for each of these parties. Ms. Salt's office is the last to sign off on the documents because they are responsible for finalizing the ordinance and resolution. A draft of the ordinance is prepared by bond counsel then reviewed and finalized by Ms. Salt. At the end of this process, the documents will all be assembled and sent to the City Council to begin the approval process, but it is important to note that until all documents are finalized and sent to the Council, the documents attached to the 1472 form may be continuously swapped out for updated versions by the different reviewers. The finalized versions sent to the Council will be the most up-to-date.

To begin the City Council approval phase, the assembled documents are sent to the City Council's docketing coordinator. The Council's docket is prepared on Thursday before the Monday and Tuesday meetings. In order to get on the docket, documents must be submitted two weeks before the Thursday before the Monday or Tuesday meeting at which they will be discussed. The docket coordinator insures that all necessary documents are attached, signed, and in order before sending them to the City Clerk's office to be docketed.

On Thursdays before Council meetings, the City Clerk prepares a binder for the Council providing information on all agenda items for the next week. Also on Thursdays before meetings, there is a briefing where Council aides are briefed on items on the upcoming docket and are able to ask questions related to those items. A similar briefing takes place on Fridays when department representative brief the City Manager or an assistant City Manager on the docketed items. On Mondays, the City Attorney office conducts an internal briefing where the City Attorney will be advised on any legal issues that may be implicated by the docketed items.

Council hearings begin on Mondays and the Brown Act requires that the Council's agenda be posted at least 72 hours prior to the hearing. If a bond issuance has been brought before the Council through the process described above, the Council will vote on it during these hearings. If the issuance is approved and if it is a negotiated sale, underwriters will then begin working on pricing the bonds.

Once a bond issuance ordinance or resolution is approved by the City Council, there is still room for modification of the bond documents and OS. An ordinance will, by its language, authorize the City Manager to make necessary, non-substantive changes to the documents. A resolution approving an OS will authorize the City Manager, City Attorney, or bond counsel to make such changes as needed, usually meaning updates to the OS.

At the end of this approval process, Ms. Salt insures that all City-prepared documents are provided to bond counsel pursuant to the closing transcript and certifications are executed by the relevant parties.

*The Public Facilities Financing Authority ("PFFA").* The bond approval process described above is a necessary component of any issuance on behalf of the City of San Diego. It is extremely important to note, however, that the City does not and cannot issue most kinds of bond debt. Instead, bonds issued for the benefit of the City must be nominally issued by one of the City's financing authorities, most often, the PFFA. The PFFA is structured as a conduit and does not have any assets. Any Master Installment Purchase Agreements executed send everything back to the City of San Diego.

The PFFA is a joint-powers authority composed of the City and the Redevelopment Agency of the City of San Diego. The Redevelopment Agency was chosen to help form this authority because it was convenient at the time the PFFA was formed. The PFFA is governed by a Board of Commissioners originally composed of the City Manager, the City Auditor and Comptroller, and the City Attorney. Its composition was first amended to remove the City Attorney and add three members of the public appointed by the Mayor and approved by the City Council. It was later amended again to remove the City Manager and City Auditor and Comptroller and to add the City Treasurer and the Executive Assistant Director of the Redevelopment Agency.

Since 1993, it has been Ms. Salt's responsibility to prepare the Board's agenda and meeting minutes, and to provide notice for PFFA meetings in accordance with the Brown Act. Once local newspaper, *The Reader*, has requested notification of meetings. Notices of the meetings have been sent in accordance with its request. Prior to their meetings on bond issuances, Ms. Salt provides the Board with the same documents provided to the City Council for its approval. The Board is not briefed the way the City Council is, but if they have any questions they call Ms. Salt. Additionally, if Ms. Salt thinks there is something in particular that the Board needs to know, she will call Board members to inform them.

The PFFA Board maintains its own agenda and minutes and votes on its own resolutions. The PFFA always takes action after the City Council has approved a matter and action is taken anywhere from several hours to a few weeks later. The PFFA's timing on reviewing a matter is dependant on Board members' schedules. PFFA Board meetings are generally held at City Hall and are open to the public. At meetings, the appropriate people from Financing Services and other relevant departments give oral reports to the Board on the proposed financing. The Board tends to ask tough questions and at least two members of the Board were involved in banking; currently, one is.

*The Board acts to approve an issuance and OS only through resolution.* These resolutions contain the same language as City Council resolutions with regard to authorized changes by the City Manger, City Attorney, or bond counsel after approval. The Board has the legal authority to question, edit, or modify the OS, but only once has the Board requested a specific language change. In that one case, a Board member who had expertise in environmental matters requested a non-substantive change related to the environmental language in an indenture.

Once the Board votes and approves an offering, the bond issuance continues along the timeline required for City Council ordinance approval. Once the ordinance is effected, bonds are then ready to be priced. Usually, an ordinance will include a maximum authorized interest rate, but pricing is discretionary. After bonds are priced, closing typically takes place within a week or two. It is important to note that in addition to all of the steps described above for the City Council and the PFFA Board, there may be some additional, treasury-required steps.

As mentioned above, the Board is a joint powers authority created under California Government Code §6500. Under that Code section, the Board members do have auditor duties but they also have complete indemnification for their official actions through the City. The San

Diego City Charter §42(b) also provides indemnification for Board members. Ms. Salt noted that the Board members are adamant that they have done nothing wrong.

*Other bond-issuing authorities.* San Diego's bond-issuing authorities include the PFFA, the Facilities and Equipment Leasing Corporation ("FELC"), the Convention Center Expansion Financing Authority ("CCEFA"), and the City/MTDB Board - the City/Metropolitan Transit Development Board.

The FELC is a non-profit public benefit corporation of which the City is the sole corporate member. Its Board is comprised of the City Manager, the City Auditor and Comptroller, and the City Attorney. The current City Attorney has chosen not to attend FELC Board meetings because of his perceived potential conflict of interest. General Counsel to this Board is Larry Marshall at Foley & Lardner.

The CCEFA is a joint powers authority made up of the City and the San Diego Unified Port District. Its Board is comprised of the City Manager, the Mayor, the Executive Director of the Port District, and the Chair of the Port District Board.

The City/MTDB is a joint powers authority made up of the City and the Metropolitan Transit Development Board. The Mayor appoints and the City Council approves two members of the public to sit on this Board. The third member of this Board is the City/MTDB Board chair.

Ms. Salt insures that each of these issuing authorities holds annual meetings in accordance with the Joint Powers Authority Act. At these annual meetings, the boards approve their budgets with respect to their bonds. Any other meetings are scheduled as needed.

*Dirt Bonds.* So-called "dirt bonds" are technically debt issued by special districts formed in each instance by the City Council. The City Council then serves as the legislative body of each district. Two reassessment districts were formed pursuant to 1915 acts. These districts were compilations of districts when bonds had been refunded. In addition to the assessment district, the City has formed two community facilities districts for which bonds have been issued. These districts are Community Facilities District (CFD) 1 - Miramar Ranch North, and CFD 2 - Santaluz. Several other CFDs have been formed but have not yet issued bonds. These are CFD 3 - Liberty Station, CFD 4 - Black Mountain Ranch, and CFD 5 - Black Mountain Ranch North.